

California Debt and Investment Advisory Commission

Fundamentals of Debt Financing

Role of the Financial Advisor



William W. Reynolds
Gardner, Underwood & Bacon LLC

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Why use a Financial Advisor?

- **The key role of an independent financial advisor is to serve as an advocate for the issuer and provide the issuer with the information necessary to make intelligent, informed decisions.**

- **Public agencies often use a financial advisor (FA) to:**
 - **Prepare financing plans and studies**
 - **Monitor outstanding debt portfolios**
 - **Develop transaction structuring options**
 - **Coordinate the bond issuance process**
 - **Serve as an issuer's "Bond Market" expert**
 - **Provide pre- and post-pricing analyses**
 - **Bid the investment of bond fund proceeds**



Financial Advisor Qualifications

- **FA should demonstrate:**
 - **Proven experience with similar issuers**
 - **Expertise with a particular type of assignment**
 - **Knowledge of financing techniques and products**
 - **Knowledge of the Bond Market**
 - **Technical competence**
 - **Availability of market resources**
 - **Ability to dedicate time and resources to the assignment**



The Role of a Financial Advisor

- **Should be an independent consultant**
 - **No underwriting**
 - **No investment management**

- **Should be an individual or firm that:**
 - **Understands your debt profile and financial history**
 - **Respects your agency's financial philosophy, goals and objectives**
 - **Can guide you through the sale process**
 - **You trust to be your financial advocate**



When Do You Use a Financial Advisor?

■ Special projects

- Debt profile/capital financing program review
- Studies/policy development
- Cash flow/debt capacity analyses

■ Bond Financing

- Develop a Plan of Finance
- Supplement staff as the bond issue coordinator
- Protect issuer's financial interest during process

The FA is an independent and objective expert of the municipal bond industry



Plan of Finance and Debt Structure

- **Establish objectives:**
 - Policies
 - Financial goals
- **Understand project scope:**
 - Cost
 - Timing
 - Funding sources
 - Source of debt repayment
- **Determine appropriate debt structure:**
 - Term
 - Debt capacity
 - Financing Vehicle
 - Bond/COP
 - Fixed/variable rate
 - Taxable/tax-exempt
 - Insured/uninsured



Selection of Financing Participants

- The financial advisor will assist with the selection of additional financing team members as required:
 - Bond Counsel/Disclosure Counsel
 - Underwriter (if negotiated)
 - Underwriter's Counsel (if negotiated)
 - Others (such as trustee, verification agent, printer, etc.)



Type of Sale

- The financial advisor will assist in determining the appropriate sale process (negotiated or competitive) based on financing particulars:
 - Issuer (frequent or infrequent) and market presence
 - Type of financing
 - Complexity of bond structure
 - Fixed vs. variable rate
 - Credit quality
 - Market conditions
 - Issue size

Competitive Sale

- **Competitive Sale - The sale of an issue through a competitive bidding process. The winning underwriter is selected by submitting the best sealed bid according to the requirements specified in the published notice of sale.**
- **FA coordinates the bond structuring and issuance process**
- **FA facilitates the competitive bidding process**
 - **Trend towards Electronic Bidding**
 - **Various Platforms - Bloomberg, Parity or Muniauction**
 - **Pros**
 - **Faster, more reliable**
 - **Ease of use**
 - **Risks**
 - **Failure of electronic system**
 - **User error**
 - **Security**

Negotiated Sale

- **Negotiated Sale – A sale of bonds whose terms and price are negotiated through an exclusive agreement with a previously selected underwriter.**
- **Use of FA varies**
 - **Good to hire a FA if issuer does not have a large finance department**
 - **Issue specific**
 - **Hire in conjunction with an underwriter**
 - **Understands issuer's overall policy goals**
 - **Have similar role as in a competitive sale**
 - **Hire to simply negotiate bond terms and pricing with underwriter**



Document Preparation

- **Financial advisor will review and assist with the preparation of all necessary documents:**
 - **Coordinate with Bond Counsel on the preparation of legal documents**
 - **Review all drafts of legal/disclosure documents**
 - **For a competitive sale, draft or assist in the preparation of the Notice of Sale and Preliminary Official Statement**



The Ratings Process

■ Assist the issuer in:

- Determining which rating agencies are appropriate
- Reviewing historic experience with agencies
- Defining nature of current and future requirements
- Consideration of investor perceptions

■ Presentations:

- Articulate themes
- Market issuer and financing
- Prepare presentation document

■ Develop a comprehensive strategy:

- Establish credit rating goals and objectives
- Analyze and understand regional factors
- Development of financial management policies
- Coordinate subsequent negotiations

Pre-Pricing Information

- FA will create an ongoing dialogue with bankers and underwriters (traders) including:
 - Gaining a knowledge of competing supply pressures, market volatility, and the economic calendar
 - Reaching a consensus on scale and structure
 - A review of market and rates in days leading to pricing
 - Facilitating pricing calls as needed during the order period
- FA will communicate pricing expectations to financing team
 - Evaluate forward calendar
 - Analyze pricing performance of recent and similar issues



Pricing Day

- Provide details on competing/comparable transactions
- Analyze any proposed changes in rates/structure
 - Redemption provisions
 - Use of premiums or original issue discounts
- Review and advise on proposed rates and underwriter's discount



Post Sale Follow-up

- Assist with closing
- Determine success of transaction
 - Market indices
 - Comparable financings
- Evaluate success of the process
 - Performance of individual firms
 - Compensation of individual firms
- Prepare Pricing Book



Compensation

■ Bond Issues

- FA's normally receive a flat fee rather than a percentage of the bond issue

■ Other Assignments

- Fixed Fee
- Hourly Fee/Capped
- Retainer
- Retainer with transaction fees



Always Remember...

The Financial Advisor is your Friend!